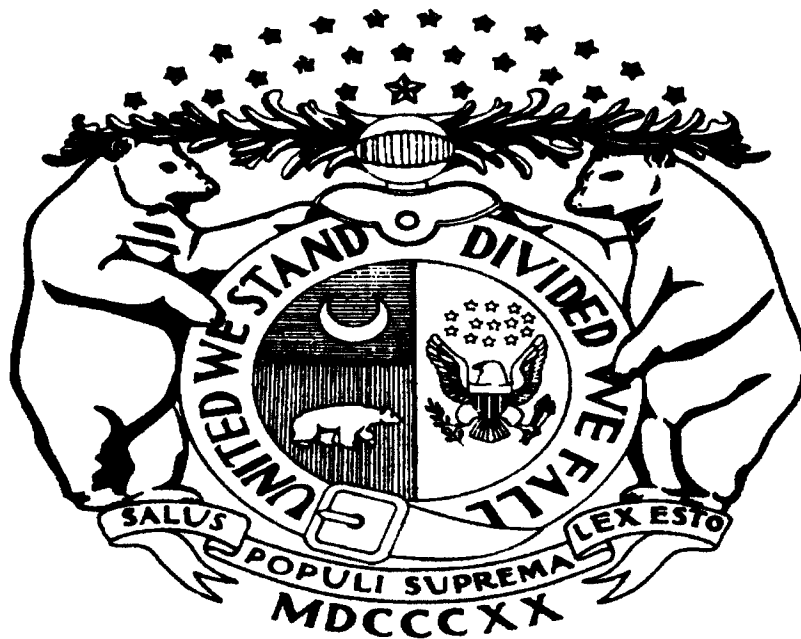


REPORT OF  
ASSOCIATION FINANCIAL EXAMINATION

**COMMUNITY HEALTH PLAN**

AS OF  
December 31, 2004



STATE OF MISSOURI  
DEPARTMENT OF INSURANCE  
JEFFERSON CITY, MISSOURI

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St. Joseph, Missouri  
June 1, 2005

Honorable Kevin M. McCarty, Commissioner  
Office of Insurance Regulation  
Florida Department of Insurance  
Chairman, (E) Financial Condition Committee

Honorable Jorge Gomez, Commissioner  
Wisconsin Department of Insurance  
Midwestern Zone Secretary

Honorable W. Dale Finke, Director  
Missouri Department of Insurance  
301 West High Street, Room 530  
Jefferson City, Missouri 65101

Gentlemen:

In accordance with your financial examination warrant, a full scope association financial examination has been made of the records, affairs and financial condition of

**Community Health Plan**

hereinafter referred to as such, as the “Company” or as “CHP.” Its administrative office is located at 137 North Belt, St. Joseph, Missouri 64506, telephone number (816) 271-1247. This examination began on February 28, 2005, and concluded on the above date.

**SCOPE OF EXAMINATION**

**Period Covered**

The prior comprehensive financial examination of Community Health Plan was made as of June 30, 2002, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC).

The current full scope association financial examination of the Company covers the period from July 1, 2002, through December 31 2004, and has been conducted by examiners from the State of Missouri representing the Midwestern Zone of the NAIC with no other zones participating.

This examination was conducted concurrently with the examination of the Community Health Plan Insurance Company, an affiliate.

This examination also include the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

### **Procedures**

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance (MDI) and statutes of the State of Missouri prevailed.

The Company's independent auditor is BKD, LLP of Kansas City, Missouri. The audited statutory financial statements for 2004 were not issued until the end of our examination fieldwork; therefore, examiners relied upon information supplied by BKD, LLP for its audit covering the period from January 1, 2003, through December 31, 2003. Information relied upon included fraud questionnaires and narrative descriptions of processes and controls.

### **Comments-Previous Examination**

Listed below are notes, comments and recommendations of the previous examination report dated as of June 30, 2002, and the subsequent response or action

taken by the Company.

## **Management**

*Comment:* The Company was directed to abide by the provisions of its Bylaws by constituting a functioning Executive Committee. The Company was also in violation of its Bylaws with respect to officers by not electing an individual to the position of Chief Operating Officer as required by its Bylaws. The Company was directed to operate according to the provisions of its Bylaws or amend the Bylaws, if a change in the management structure was desired.

*Company Response:* An Executive Committee was appointed but had no occasion to meet during the audit period. Should a meeting be called, minutes will be kept and available for exam purposes. The Chief Operating Officer was elected on November 21, 2002 as required by the Bylaws.

*Current Findings:* It was noted that the Company did appoint an Executive Committee and a Chief Operating Officer during the period under examination.

## **Conflict of Interest**

*Comment:* Neither the board members nor the officers of CHP completed conflict of interest statements in 2001. Problems had been noted in the last three examinations of the Company in this area. It was strongly advised that the Company cure these recurring exceptions by requiring each officer and director to execute a statement of conflict of interest annually.

*Company Response:* Conflict of interest statements were obtained in June 2000 and again in January 2002. Since there were no changes in the membership of the board or the officers in 2001, new statements were not obtained. Every effort will be made to obtain conflict of interest statements every year from all appropriate parties.

*Current Finding:* Conflict of interest statements were obtained from officers and directors for the years under examination.

## **Corporate Records**

*Comment:* The minutes of the board of directors did not appear to properly reflect and approve the corporate transactions and events for the period under examination. It was noted that the board of directors did not approve, via a motion, the reports of its various committees. It was directed that the board of directors specifically approve reports of committees of the board and that such approval be reflected in the board minutes.

*Company Response:* The reports of individual standing committees of the board will be approved at each board of directors' meeting and duly noted in the minutes. If a committee does not meet in a particular month, this will be noted in the minutes.

*Current Finding:* The board properly approved all committee meeting minutes and actions and noted in the minutes when a committee did not meet.

#### **Intercompany Transactions – Office Lease Agreement**

*Comment:* The Company began paying a different amount for rent without obtaining prior approval of the MDI. The Company was directed to desist from paying a different amount for rent until prior approval of the MDI is obtained.

*Company Response:* The lease has been renegotiated and filed and approved by MDI.

*Current Finding:* The office lease was amended effective July 1, 2002, July 1, 2003, and July 1, 2004 to change the monthly rental amounts. Each of these amendments were properly filed with the MDI.

#### **Insurance Products and Related Practices – Provider Contracts**

*Comment:* The Company was not in compliance with Section 376.1077(1) RSMo, (Administrator to have agreement with insurer, form, contents-termination, how) as it was unable to provide an underlying agreement with Allianz Life Insurance Company (Allianz) for its Third Party Administrator (TPA) functions. CHP was directed to enter into a written agreement with Allianz, specifying its rights and obligations as an administrator of accidental death and dismemberment coverage.

*Company Response:* The Company did not provide a response to this prior recommendation.

*Current Finding:* CHP provided an agreement with Allianz for its administrator functions under the agreement to sell group policy life insurance.

*Comment:* The Company had not filed various provider agreements with the MDI as required under Section 354.624 RSMo, (Proposed provider contract forms filed with the Director). The Company was directed to file these agreements.

*Company Response:* The Company filed the three contracts listed and received approval to use them in Missouri. The Company will see that all provider contracts are based upon approved forms.

*Current Finding:* It was noted that the agreements in question had in fact been filed with and approved by the MDI in February 2000.

*Comment:* Caremark, Inc. was acting as a TPA within the provisions of Section 376.1075(1) RSMo, (Definitions) in its capacity as the pharmacy benefits manager for the Company without a TPA license in Missouri as required within the provisions of Section 376.1092 RSMo, (Certificate of authority, required, application, contents, fee). The Company was directed to cause Caremark to comply with all the applicable Missouri laws in this regard.

In addition, Caremark, Inc. was not registered as a Utilization Review Agent (URA) with the Missouri Department of Insurance and was not covered by the exemptions listed in Section 374.500(6) RSMo, (Definitions). However, Caremark, Inc. was performing utilization review services for CHP as the pharmacy benefit manager. CHP was directed to cause Caremark to obtain a URA license in Missouri in order to perform its obligations under the contract.

*Company Response:* The Company terminated its contract with Caremark as of December 31, 2002. The new PBM, PharmaCare Management Services, Inc. (PharmaCare), has been advised that both TPA and URA licenses will be required in Missouri.

*Current Findings:* CHP terminated its contract with CareMark, Inc. effective December 31, 2002 and entered into a new agreement with PharmaCare effective January 1, 2003. It was noted that while PharmaCare was a licensed TPA for the state of Rhode Island where it is located, PharmaCare does not have a TPA license in the state of Missouri. See the Insurance Products Section of this report for recommendations.

## **Reinsurance**

*Comment:* The Company had been cited in the last three examinations regarding its failures to comply with the laws and regulations regarding reinsurance agreement filings with the MDI. The Company was directed again, to file all reinsurance agreements with the MDI within the time limit provided by statute.

*Company Response:* CHP will file its new and renewal reinsurance contracts with the MDI, as required. This item has been added to the Company's checklist of required filings in an effort not to overlook this requirement.

*Current Findings:* Company complied with the laws and regulations regarding reinsurance agreement filing with the MDI for all years under examination.

## **Health Care Receivable**

*Comment:* The Company did not follow Statement of Statutory Accounting Principles (SSAP) No. 84 as it related to this account and in the process over-estimated the amount admissible under current standards. The Company was directed to keep current with changes in statutory accounting principles and ensure that amounts reported in the Annual or Quarterly Statements are accurate.



*Company Response:* Effective with the third quarter 2002 statement filing; Pharmaceutical rebates receivable counted as admitted assets will not exceed three months of age.

*Current Finding:* Although there were some immaterial items misclassified as Health care receivables, the overall amount reported appeared reasonable and was determined in accordance with applicable SSAPs.

### **Claims Unpaid and Unpaid Claims Adjustment Expense**

*Comment:* The Company improperly combined the amount attributable to the unpaid claims adjustment expenses into the unpaid claims account. The Company was directed to separately report these items in its future Annual and Quarterly Statements.

*Company Response:* Unpaid claims adjustment expenses will be reported separately from Unpaid claims on future statement filings.

*Current Findings:* The Company has complied with the prior recommendation by separately reporting Unpaid claims adjustment expenses.

### **General Expenses Due or Accrued**

*Comment:* CHP did not properly accrue for various account payable items as of the examination date. The Company was advised to properly accrue for all expenses that are due and payable at statement dates.

*Company Response:* CHP will make every effort to accrue adequate liabilities at period ends for expenses incurred on or before the applicable period end.

*Current Finding:* The year-end accruals for items payable as of December 31, 2004, appeared reasonable.

### **Subsequent Event**

*Comment:* CHP was appointed as an administrative services organization by Heartland to administer Heartland's self-insured health plan for its employees pursuant to a management agreement. The management agreement was not filed with the MDI in accordance with Section 382.195 (1), RSMo (Transactions within a holding company system). CHP was directed to file this agreement with the MDI immediately.

*Company Response:* The agreement in question has been filed with and approved by the MDI.

*Current Finding:* The Company complied with the prior recommendation by filing the agreement.

## Capital and Surplus Issues Going Forward

*Comment:* In accordance with the requirements of Section 354.5512 (2) RSMo, (Point of Service Riders), CHP was insolvent as of June 30, 2002, due to insufficient surplus. Additional adjustments made as a result of the prior examination further reduced the Company's surplus. Subsequent to the prior examination date, Heartland made addition surplus contributions totaling \$400,000 to increase CHP's surplus levels. However, these additional contributions were eroded by subsequent operating losses. Given that CHP relies heavily on contributions from Heartland to maintain minimum surplus requirements due to operating losses, it was directed that:

- The level of surplus contributions by Heartland be increased both in amount and in frequency in order to eliminate the possibility of CHP falling into insolvency status, which could trigger serious regulatory action by the MDI.
- CHP should prepare an estimate of future operating losses based on historical operational data and pre-fund the estimated losses in order to cure the recurring deterioration of surplus.
- CHP should seriously consider re-instituting the Global Capitation Agreement with Heartland Regional Medical Center which limited its losses for certain insured employer groups.

*Company Response:* Capital contributions have been increased in line with MDI recommendations. The current approved budget plus concurrent monitoring of operating results are being used monthly for estimating losses and capital contribution requirements. The Company notes the recommendation relating to the Global Capitation Agreement, but respectfully declines to enter into such an agreement at this time.

*Current Finding:* The Company's surplus position has increased significantly subsequent to the prior examination date. The improvement is the result of additional contributions made by Heartland in the last half of 2002 and to operating gains the Company experienced in 2003 and 2004. These operating gains are primarily the result of rate increases and the transfer of Heartland employees to a self-funded plan.

## HISTORY

### General

Community Health Plan, a not-for-profit corporation, was incorporated under the laws of the State of Missouri on September 8, 1994. A Certificate of Authority to operate as a Health Maintenance Organization (HMO) was issued by the State of Missouri on December 29, 1994, and the Company commenced business on July 1, 1995. Effective

December 6, 1996, the Company received a Certificate of Authority to transact business from the State of Kansas.

CHP is a wholly owned subsidiary of Heartland Health (Heartland). Heartland is a not-for-profit organization, and is the parent of Heartland Regional Medical Center of St. Joseph, Missouri, and various other health care related entities.

### **Capital Stock and Dividends**

CHP is organized as a not-for-profit corporation, and consequently, does not have any capital stock and does not declare or pay any dividends. The ownership interest of Heartland in CHP is authorized in the Company's Articles of Incorporation.

### **Management**

The management of CHP is vested in a board of directors that is appointed by the sole owner, Heartland Health. The directors of CHP elected and serving as of December 31, 2004, were as follows:

<u>Name and Address</u>	<u>Business Affiliation</u>
Charles William Salanski St. Joseph, Missouri	Retired
Alan Wayne Brewer, DO Faucet, Missouri	Practicing Physician Heartland Health
Lowell Charles Kruse St. Joseph, Missouri	President & CEO Heartland Health
William David Miller, MD St. Joseph, Missouri	Practicing Physician Family Medicine Associates
Scott Michael Folk, MD St. Joseph, Missouri	Practicing Physician Heartland Health

Ryne Patterson Lilly St. Joseph, Missouri	Executive Director St. Joseph Chamber of Commerce
Patrick Charles Dillon St. Joseph, Missouri	Owner The Dillon Company
Frank Anthony Leone St. Joseph, Missouri	General Manager City Car Chrysler
Jean Brown St. Joseph, Missouri	Executive Director St. Joseph YWCA
Mary Cotter St. Joseph, Missouri	Realtor Coldwell Banker

The Company's Bylaws specify the number of directors of the Company is to be eleven; however, due to the death of one of the directors in 2004, as of December 31, 2004, the number of directors was only ten. Effective January 1, 2005, John Jarrett of St. Joseph, Missouri was appointed to replace Larry Jones who had passed away in June 2004.

The Company's Bylaws specify that the Company shall have the following committees: Executive, Finance, Provider Relations/Credentialing, and Marketing. In addition, the Chairman of the Board may establish special committees as needed. As of December 31, 2004, the only committees in operation were those specifically required by the Bylaws.

Pursuant to its Bylaws, the officers of the Company shall be a President (Chief Executive Officer), a Chief Operating Officer, a Secretary, a Chief Financial Officer (Treasurer), and such other officers and assistant officers as may be deemed necessary. The officers elected and serving, as December 31, 2004 were as follows:

<u>Name</u>	<u>Title</u>
Lowell Charles Kruse	President & Chief Executive Officer
Curt Kretzinger	Chief Operating Officer
Rudy Wacker	Chief Administrative Officer
John Paul Wilson	Secretary/Treasurer & Chief Financial Officer
Edna Marie Everly	Assistant Secretary
Douglas Martin Brandt	Assistant Treasurer

### **Conflict of Interest**

The Company has procedures, which require all officers and directors complete a conflict of interest statement annually. Signed conflict of interest statements were reviewed for the examination period, and no significant conflicts were disclosed.

### **Corporate Records**

A review was made of the Articles of Incorporation and Bylaws for the examination period. The Bylaws were revised effective December 18, 2002. The changes consisted of some clarifications relating to annual meetings and responsibilities of committees as well as the removal of language regarding the initial board of directors.

The minutes of the Company's board of directors and the various committee meetings were reviewed, and in general, appear to properly reflect and approve the corporate transactions and events for the period under examination.

### **Acquisitions, Mergers and Major Corporate Events**

Effective August 1, 2002, approximately 5,000 member-insureds who were employees of Heartland Health were transferred to a self-insured plan sponsored by Heartland. CHP was contracted by Heartland to become the administrator of the plan, functioning as an Administrative Service Organization (ASO) pursuant to a management agreement discussed in greater detail in the Intercompany Transactions section of this

report. The members transferred to the self-insured plan represented approximately 25% of CHP's total membership as of the transfer date.

In March 2003, Heartland Health acquired A.G. Edwards Life Insurance Co., which immediately upon acquisition changed its name to Community Health Plan Insurance Company (CHPIC). CHPIC was purchased so that a PPO product could be offered to subscriber groups in conjunction with the HMO products being offered by CHP. Subsequent to the purchase, CHP and CHPIC entered into a Dual Option Product Agreement, which is discussed in greater detail in the Intercompany Transactions section of this report.

### **Surplus Debentures**

As of December 31, 1999, CHP had \$21,112,460 in surplus notes, comprised of \$19,950,000 in principal and \$1,162,460 in accrued interest, all due and payable to Heartland. Effective June 30, 2000, pursuant to an action of the Heartland board of directors, which was approved by the MDI, the principal balance of the outstanding surplus notes was converted to contributed surplus. Therefore, only \$1,162,460 in accrued interest remained in CHP's surplus notes account as of December 31, 2004. Any repayment of this accrued interest must receive the prior approval of the Director of the MDI.

## **AFFILIATED COMPANIES**

### **Holding Company, Subsidiaries and Affiliates**

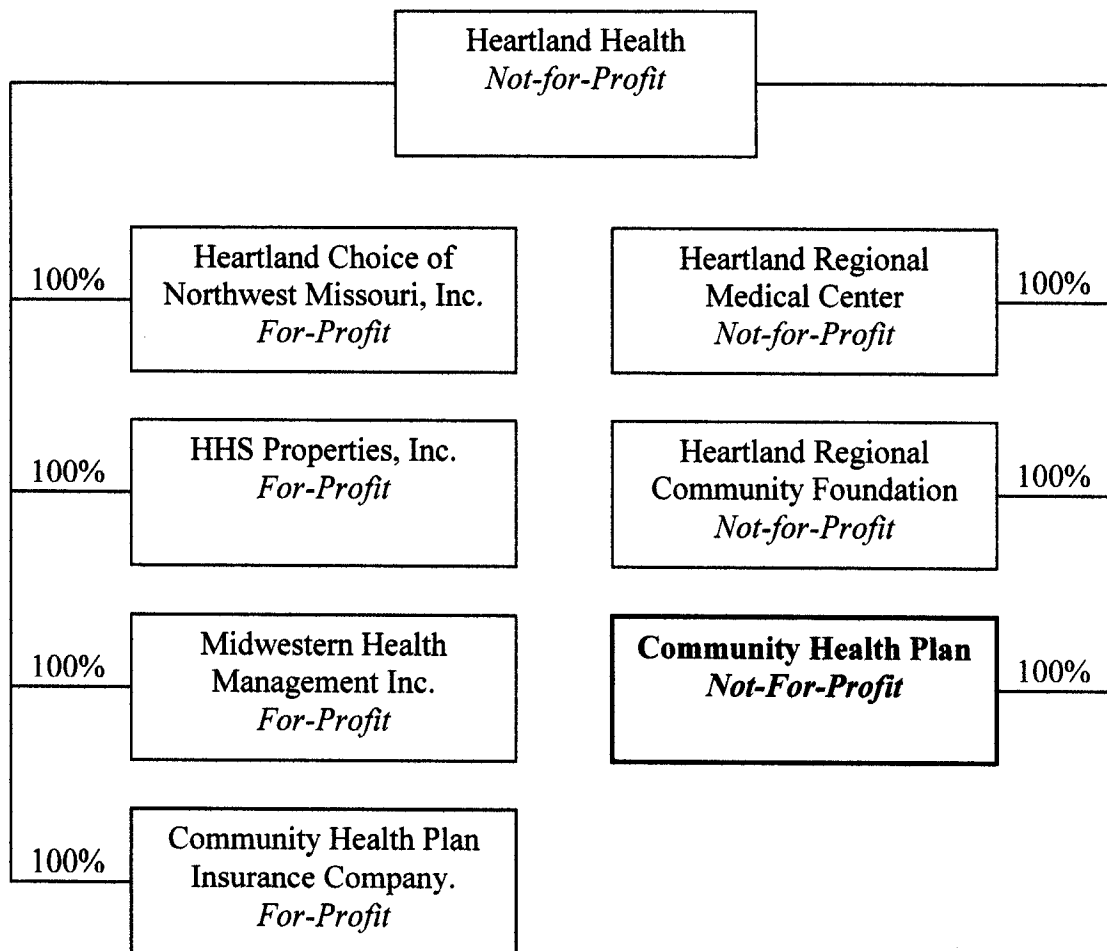
Community Health Plan is a wholly owned subsidiary of Heartland Health. CHP is a member of an insurance holding company system as defined by Section 382.010

RSMo (Definitions). Insurance Holding Company Registration Statements were filed by Heartland, on behalf of CHP and its insurance affiliate, CHPIC, for the period under examination.

Heartland is a Missouri not-for-profit and community-based health care organization. It was comprised of eight companies as of December 31, 2004. All of the companies operate in, or are related to, the health care industry.

### **Organizational Chart**

The following organizational chart depicts the holding company system including CHP as of December 31, 2004:



### **Intercompany Transactions**

The Company was a party to various intercompany agreements with related parties as of December 31, 2004. These agreements are summarized as follows:

1. Type: Administrative Services Allocation Agreement

Parties: CHP and Heartland Health

Effective: Retroactive to December 29, 1994

Terms: Heartland provides various administrative services to CHP. A pro-rata share of the cost of the following services are charged to CHP each month: human resources management, employee benefit administration, payroll processing and accounts payable processing, purchasing and central supply, general ledger accounting, data processing management, financial (including tax) planning and management, education and training, and internal consulting/special projects.

In addition, 100% of the cost of the following items are reimbursed to Heartland by CHP: (a) salaries, payroll taxes, and fringe benefits and (b) accounts payable payments. The “accounts payable payments” specifically include: professional fees and purchased services; supplies, dues and subscriptions; insurance, utilities, repair and maintenance; travel, education, and training expenses; and all other CHP expenses paid through accounts payable.

Exception: CHP has a nurse advice Call Center for the benefit of members who may have questions or need assistance. The Call Center is providing various services to Heartland Regional Medical Center and related clinics without the benefit of a written agreement. The charges for these services are offset against the amounts owed to Heartland under the Administrative Services Allocation Agreement. The Company is directed to obtain a written agreement for the provision of the Call Center services. The agreement should clearly indicate the types of services to be provided, how charges are to be determined and manner of payment. The agreement should then be filed with the MDI for approval as required by Section 382.195 RSMo (Transactions Within a Holding Company System).



2. Type: Administrative Service and Network Access Agreement  
  
Parties: CHPIC and CHP  
  
Effective: July 1, 2003  
  
Terms: CHP will provide administrative, management and support services to CHPIC. These services shall include: finance, accounting, information systems, marketing, purchasing and medical claims benefits. CHP shall also provide CHPIC with access to its network of contracted health care providers. For the provision of these services, CHPIC shall pay CHP a monthly fee equal to 12% of premiums received by CHPIC.
3. Type: Dual Option Product Agreement  
  
Parties: CHPIC and CHP  
  
Effective: January 1, 2004  
  
Terms: CHPIC and CHP agree to offer a dual option health benefit program jointly to employer groups of 26 or more employees. CHP shall offer a HMO product and CHPIC shall offer a PPO product. The individual employees of each employer group shall elect which benefit program shall apply to them. Premiums shall be recorded by actuarially established rates on the books of each party, and medical expenses incurred under the dual option programs will be charged to the books of the respective company responsible for the benefit program chosen by the employee. On at least a quarterly basis, the net income or net loss of each group under the dual option program will be computed and split equally between CHP and CHPIC.
4. Type: Administration Agreement  
  
Parties: CHP and Heartland  
  
Effective: July 1, 2004 and expires June 30, 2005  
  
Terms: CHP shall provide claims processing and related administrative services to Heartland relating to Heartland's Employee Benefit Plan. CHP shall receive a fee of \$83.99 per employee per month for providing these services. Within 30 days of the last day of the contract term, a true-up of costs will be computed based on the actual average per member per month administration costs to CHP. The parties will then settle any over or under payments within 15 days of calculation of the true up amount.

**Exception:** It was noted that the Company was reporting the fees received from the Administration Agreement as a write-in item under aggregate write-ins for other health care related revenues on the Statement of Revenue and Expenses. Per SSAP No. 47, Paragraph 5, all income and expenses related to claims, losses, premiums and other amounts received or paid on behalf of self-insured plans are to be excluded from the administrator's statement of operations. The administration fees should have been reported on line 19 (Reimbursements by uninsured accident and health plans) of Part 3 of the Underwriting and Investment Exhibit as an offset to expenses. Although the administration fees received were considered material for our examination purposes, an examination change will not be made to reclassify the administration fees since such a reclassification would not effect CHP's ending surplus. However, the Company should ensure that the administration fees are properly reported on future Annual and Quarterly Statement filings.

The Administration Agreement does not address how rebates received on pharmacy claims paid on behalf of the Heartland Employee Benefit Plan should be handled. Currently, these rebates are retained by CHP. The Company should amend the Administration Agreement to clarify the handling of pharmacy rebates.

5. **Type:** Office Space Lease Agreement

**Parties:** CHP and Heartland

**Effective:** Original lease agreement was effective July 1, 2002. Exhibit 'A' to the agreement was amended effective July 1, 2003 and July 1, 2004, to adjust the base rent amounts.

**Terms:** CHP agrees to lease office space and office equipment and furniture from Heartland. The monthly amount of the base rent is set by Heartland at the beginning of each fiscal year (July 1), by an amendment to Exhibit 'A', and is payable by CHP before the end of the month following the month of occupancy.

6. **Type:** Lease Agreement

**Parties:** CHP and Heartland Regional Medical Center (HRMC)

**Effective:** January 1, 2004.

**Terms:** Under a separate lease agreement which expired August 31, 2004, CHP paid HRMC \$58,000 per month to lease the Erisco Facets Software System, which CHP uses for its business operations. The lease agreement which became effective January 1, 2004, is for upgrades to

the software system. Under the agreement, CHP is entitled to use the software upgrades for its business operations at a monthly rental of \$14,153 over a five-year period for a total of \$849,205.

7. Type: Participating Hospital Agreement

Parties: CHP and HRMC

Effective: July 1, 1995, the agreement has been amended numerous times usually to adjust discounts on per diem rates.

Terms: HRMC shall provide hospital services to CHP members when services are provided by physicians or other licensed health care professionals with the requisite privileges at HRMC. HRMC is to be reimbursed by CHP the applicable per diem as set forth in Attachment “A” of the agreement subject to percentage discounts. Per an Amendment effective July 1, 2004, CHP receives a discount of 34.3% off charges for billed inpatient and outpatient services.

Exception: The July 1, 2004 Amendment and a change to the discount rate made per a memorandum effective July 1, 2003 were not filed for prior approval with the MDI as required by Section 382.195 RSMo. The Company is directed to file the July 1, 2004 Amendment with the MDI and ensure amendments to intercompany agreements are properly filed in the future.

8. Type: Consulting Physician Agreement

Parties: CHP and Heartland Regional Medical Center d/b/a Medical Group Practice (MGP)

Effective: September 1, 2004

Terms: MGP shall provide appropriate covered services to CHP members in the specialty area of MGP upon referral by a member’s primary care physician. CHP will compensate MGP the lesser of MGP’s billed charges or the CHP maximum fee schedule in effect as of the date of the service less any member co-pay. CHP’s maximum fee schedule utilizes the current year’s Medicare Resource Based Relative Value Scale multiplied by 120%.

9. Type: Primary Care Physician Agreement

Parties: CHP and Heartland Health d/b/a Heartland Primary Care (HPC)

Effective: January 1, 2004

Terms: HPC agrees to provide to CHP members medically necessary primary care covered services. HPC may refer members to other participating consultant physicians for services as necessary. CHP will compensate HPC the lesser of HPC's billed charges or the CHP maximum fee schedule in effect as of the date of the service less any member co-pay. CHP's maximum fee schedule utilizes the current year's Medicare Resource Based Relative Value Scale multiplied by 120%.

The amounts (paid) to and received from parent and affiliates during years under examination were as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Admin. Services Allocation Agreement			
Paid to Heartland	\$(980,701)	\$(1,090,474)	\$(1,103,368)
Admin. Service & Network Access Agreement			
Received from CHPIC	476,711	27,018	N/A
Dual Option Product Agreement			
Paid to CHPIC	(1,011,935)	-0-	N/A
Administration Agreement			
Received from Heartland	2,184,061	2,404,249	1,029,845
Office Space Lease Agreement			
Paid to Heartland	(336,918)	(423,193)	(171,910)
Lease Agreements			
Paid to Heartland	(633,825)	(695,976)	(695,976)
Participating Hospital Agreement			
Paid to Heartland	(12,973,867)	(13,113,677)	(18,274,182)
Primary Care Physician Agreement			
Paid to Heartland	(860,689)	(684,461)	(925,940)
Consulting Physician Agreement			
Paid to Heartland	(2,353,873)	(1,855,794)	(1,934,617)
Primary Care Physician Agreement			
Paid to Heartland	<u>(860,689)</u>	<u>(684,461)</u>	<u>(925,940)</u>
<b>Net amount (paid) or received</b>	<b><u>\$(16,491,036)</u></b>	<b><u>\$(15,432,308)</u></b>	<b><u>\$(22,076,148)</u></b>

CHP is also a party to a Continuation of Coverage Policy with its affiliate CHPIC.

Under this agreement, CHPIC agrees to provide continuation of care reinsurance coverage to CHP in the event CHP becomes insolvent. This agreement is discussed in greater detail in the Reinsurance section of this report.

## **FIDELITY BOND AND OTHER INSURANCE**

The Company is a named insured on a crime policy issued to Heartland Health. The policy provides coverage with a liability limit of \$1,000,000 and a \$10,000 deductible. The crime coverage for Heartland and its subsidiaries on a consolidated basis does not meet the amount suggested in guidelines promulgated by the NAIC, which is between \$1,250,000 and \$1,500,000 in coverage. The Company should ensure that if the crime coverage continues to be purchased on a consolidated basis, it be increased to meet the suggested NAIC amounts, or the Company should obtain crime coverage sufficient to meet the NAIC guidelines as a separate entity.

The Company has a Managed Care Organization Errors and Omissions policy, an Excess Managed Care policy and is also a named insured on the following insurance policies issued to Heartland: Directors and Officers Liability, Excess Commercial General Liability and Umbrella Excess Commercial General Liability.

## **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

As of December 31, 2000, and prior, employees of CHP were participants in a qualified defined pension plan sponsored by Heartland Health. Effective January 1, 2001, the plan was amended to become a 401(k) Retirement Plan on a going forward basis, with the following provisions: employees hired on or after January 1, 2001, who become eligible are restricted to the 401(k); and longer tenured employees have a choice to continue accruing benefits under the plan or switch to the 401(k). Both plans are funded by Heartland and employees may elect to defer a portion of their compensation for retirement in either plan.

Employees of CHP are provided a variety of other benefits, which include, but are not limited to, medical and dental coverage, vision coverage, life and accidental death and dismemberment coverage, paid vacation and sick leave, and education reimbursement. CHP's share of the cost of these benefits is paid to Heartland through an Administrative Services Allocation Agreement.

## **STATUTORY DEPOSITS**

### **Deposits with the State of Missouri**

The funds on deposit with the Missouri Department of Insurance as of December 31, 2004, as reflected below, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with Section 354.410 RSMo (Issuance of certificate; trust deposits and capital requirements) and Section 354.551 RSMo (Point of service riders). The funds on deposit were as follows:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
U.S. Treasury Notes	\$930,000	\$925,767	\$926,342

### **Deposits with Other States**

CHP does not have funds on deposit with any other state.

## **INSURANCE PRODUCTS AND RELATED PRACTICES**

### **General**

The Company was organized under the laws of the State of Missouri in accordance RSMo Chapter 354 (Health Service Corporations-Health Maintenance Organizations) as it relates to health maintenance organizations. CHP is licensed to

transact business in the states of Missouri and Kansas. The Company is also permitted to offer Point of Service riders (POS) with its approved health products in the state of Missouri.

The Company operates as an Individual Practice Association (IPA) model HMO which provides health care benefits to employer groups on a prepaid basis. Effective August 1, 2002, approximately 5,000 insured members of CHP who were also employees of Heartland Health, the parent company, became insured by a self-insured plan (Plan) sponsored by Heartland. CHP was contracted by Heartland to become the administrator of the Plan, functioning as an Administrative Services Organization (ASO) pursuant to an Administration Agreement discussed in greater detail in the Intercompany Transactions section of this report.

The MDI has a market conduct staff which performs a review of various market conduct issues and generates a separate market conduct report. The last Market Conduct Examination Report [#0128-10-HMO] dated June 25, 2002, reviewed the period January 1, 2000 through December 31, 2000. A cursory review of the report indicated the Company was fined by the MDI for various violations of Missouri insurance laws and regulations. The violations and resulting fines would not appear to have a material impact on the financial condition of the Company. The market conduct staff also performed a limited review of the Company's prompt pay procedures in May of 2004 as a follow up to certain issues noted in their examination. As of the date of this report, no market conduct report has been issued related to the follow up examination.

**Marketing**

The Company's marketing activities involve the use of pamphlets, brochures, newspaper, magazine and professional publications advertising. The Company also publishes a yearly newsletter, which reports health information and other health-care coverage events to its insured members.

The Company markets its products through the use of direct marketing techniques and through in-house and independent agents and insurance brokers. CHP's service area is comprised of 21 counties located in northwestern Missouri and 6 counties located in northeastern Kansas. As of December 31, 2004, CHP provided benefits to 19,345 enrollees. The Company's largest subscriber group was the Missouri Consolidated Health Care Plan, which is made up primarily of employees of the state of Missouri and represented 34% of CHP's total enrollees.

Insured members of CHP are offered group life and accidental death and dismemberment coverage underwritten by Allianz Life Insurance Company of North America (Allianz). CHP collects and remits premiums for this coverage as a licensed Third Party Administrator (TPA).

**Provider Contracts**

The Company has numerous provider agreements in place with participating hospitals, primary care physicians, consulting physicians, ancillary providers, and physician health organizations including a participating hospital agreement with its affiliate, Heartland Regional Medical Center.

Participating hospital providers are reimbursed on the basis of per diem or percentage of charges less applicable co-pays and deductibles. Consulting physicians



are reimbursed for the lesser of the actual billed charges or CHP's maximum fee schedule in effect as of the service date, minus insured co-pays. Primary care physicians are also reimbursed for the lesser of the actual billed charges or CHP's maximum fee schedule in effect as of the service date, minus the member co-pays.

The Company contracts with PharmaCare Management Services, Inc. (PharmaCare) for management of its prescription benefit to include providing a network of retail pharmacies, mail service, claims processing, customer service, formulary programs, maintaining records, and serving as a purchasing agent. PharmaCare is acting as a TPA within the provisions of Section 376.1075(1) RSMo (Definitions.) However, PharmaCare is not licensed as a TPA with the MDI as required within the provisions of Section 376.1092 RSMo (Certificate of authority, required, application, contents, and fee.) The Company is directed to cause PharmaCare to comply with all the applicable Missouri laws in this regard. CHP is further directed to comply with Section 376.1084 RSMo, (Insurer responsible for benefits and underwriting practices) regarding semi-annual reviews of TPAs.

The Company's contract with PharmaCare requires PharmaCare to also perform utilization reviews. However, PharmaCare is not registered as a Utilization Review Agent (URA) with the MDI and is not covered by the exemptions listed in Section 374.500(6) RSMo, (Definitions). The Company is directed to cause PharmaCare to obtain a URA license in Missouri in order to perform its obligations under the contract.

### **Rates**

The Company's underwriting guidelines and the underlying policies and procedures are utilized in determining rates charged to member-insureds. Insured groups

are rated based on specific demographics such as single, employee and spouse, or family. The rates charged by the major providers are summarized as part of the review of provider contracts above.

### **Grievance Procedures**

The Company has established procedures for handling both enrollee and provider complaints and grievances. The procedures, as outlined in a policy and procedures manual, appear to meet the requirements of Missouri Regulation 20 CSR 400-7.110 (Health Maintenance Organizations-Resolutions of Enrollee Grievances).

### **Quality Assurance, Utilization Review and Provider Credentialing**

The Company has procedures in place for each of these areas. CHP has a joint Provider Relations/Quality Review Committee that meets monthly to review and discuss quality management and utilization issues. This committee reviews credentialing and re-credentialing applications from prospective providers. Approved lists of credentialed providers are subsequently presented to the board of directors for final approval.

The Company has been approved to provide health care coverage to the Federal Employee Health Benefits Program, which requires the Company be accredited by the National Committee for Quality Assurance (NCQA). The Company is in the process of obtaining NCQA accreditation and anticipates that this process will be completed some time in 2006.

**REINSURANCE****General**

The Company's reinsurance and premium activity during the period under examination are as follows:

<u>Premiums:</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
Direct Business	\$62,971,085	\$56,878,835	\$60,568,234
Reinsurance Assumed	-0-	-0-	-0-
Reinsurance Ceded:			
Affiliates	-0-	-0-	-0-
Non-affiliates	<u>(341,396)</u>	<u>(553,074)</u>	<u>(832,685)</u>
Net Premiums Written	<u>\$62,629,689</u>	<u>\$56,325,761</u>	<u>\$59,735,549</u>

**Assumed**

The Company does not assume any business.

**Ceded**

The Company is contingently liable for all reinsurance losses ceded or retroceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

The Company and its affiliate, CHPIC, are both named reinsureds on a HMO Excess of Loss Risk Reinsurance Agreement effective July 1, 2004, through June 30, 2005 with Standard Security Life Insurance Company (Standard). Under the agreement, CHP cedes 90% of its eligible hospital service claims subject to a \$125,000 retention to Standard. Standard's maximum liability is limited to \$1,000,000 per member per agreement year with a maximum liability per covered member per lifetime of \$2,000,000.

The Company has a Continuation of Coverage Policy with its affiliate CHPIC effective July 1, 2004 through July 1, 2005. Under the terms of the agreement, CHPIC is to provide continuation of care coverage to CHP members in the event of CHP's insolvency. An annual premium of \$10,000 is charged under the agreement. Under a separate Guaranty Agreement between CHPIC and Heartland, Heartland unconditionally guarantees the full and prompt payment and performance of any accounts CHPIC is obligated to pay on behalf of CHP in connection with the Continuation of Coverage Policy.

## **ACCOUNTS AND RECORDS**

### **Independent Auditor**

The Company's financial statements for the year ending December 31, 2002, were audited by the CPA firm of KPMG, LLP, Kansas City, Missouri. The Company's financial statements for the year ending December 31, 2003 were audited by the CPA firm of BKD, LLP, Kansas City, Missouri, and BKD was also retained to perform the year-end 2004 statutory audit. Audited statutory financial statements for 2004 were not issued until the end of our examination fieldwork.

### **Independent Actuary**

The Company's unpaid claim reserves were reviewed and certified by Richard Johnson, FSA, MAAA, of Pavidan Benefit Services, Inc. of Minneapolis, Minnesota, for each of the years under examination.

**Custodial Agreement**

During our review of the Company's cash and investment accounts, it was noted that the Company's custodial agreements with US Bank and with Commerce Bank did not contain all of the safeguard provisions specified in Part 1, Section IV of the NAIC Financial Condition Examiners Handbook. The Company should amend or restate the custodial agreement so that it contains all of the NAIC specified safeguard provisions. Until such time as the agreement is brought into compliance with NAIC guidelines, it should be disclosed in General Interrogatory 23.02 of the Annual Statement relating to custodial agreements that do not comply with NAIC guidelines.

**FINANCIAL STATEMENTS**

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2004. Any examination adjustments to the amount reported in the Annual Statement and/or comments regarding such are made in the "Notes to the Financial Statements." (The failure of any column of numbers to add to its respective total is due to rounding or truncation.)

There may have been differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements. Therefore, they were communicated to the Company and/or noted in the workpapers for each individual Annual Statement item.

**Assets**

	<u>TOTAL ASSETS</u>	<u>NON- ADMITTED ASSETS</u>	<u>NET ADMITTED ASSETS</u>
Bonds	\$2,151,368		\$2,151,368
Common stocks	319,696		319,696
Cash and short-term investments	8,237,927		8,237,927
Investment income due and accrued	13,718		13,718
Uncollected premiums and agents' balances	2,034,875		2,034,875
Net deferred tax asset	8,874,538	\$8,458,262	416,276
Electronic data processing equipment	331,872	267,135	64,737
Furniture and equipment	146,812	146,812	-0-
Health care and other amounts receivable	127,727	60,000	67,727
Aggregate write-ins for other than invested assets:			
Prepaid expenses	<u>332,228</u>	<u>332,228</u>	<u>-0-</u>
<b>TOTAL ASSETS</b>	<b><u>\$22,570,761</u></b>	<b><u>\$9,264,437</u></b>	<b><u>\$13,306,324</u></b>

## **Liabilities, Capital and Surplus**

Claims unpaid	\$6,841,280
Unpaid claims adjustment expenses	205,000
Premiums received in advance	779,671
General expenses due or accrued	1,084,964
Current federal and foreign income tax payable	12,292
Amounts due to parent, subsidiaries and affiliates	<u>278,718</u>
<b>Total Liabilities</b>	<b>\$9,201,925</b>
Gross paid in and contributed surplus	30,900,000
Surplus notes	1,162,460
Unassigned funds (surplus)	<u>(27,958,061)</u>
<b>Capital and Surplus</b>	<b><u>\$4,104,399</u></b>
<b>Total Liabilities and Surplus</b>	<b><u>\$13,306,324</u></b>

## **Statement of Revenue and Expenses**

MEMBER MONTHS	<u>233,285</u>
Net premium income	\$62,629,689
Aggregate write-ins for other health care related revenues:	
Administration fees-point of service	2,184,061
Commissions	13,015
Call Center and other fees	<u>461,152</u>
<b>Total Revenues</b>	<b>\$65,287,917</b>
<b>Hospital and Medical:</b>	
Hospital/medical benefits	22,730,358
Other professional services	12,148,633
Outside referrals	1,620,100
Emergency room and out-of-area	3,437,172
Prescription drugs	5,203,445
Aggregate write-ins for other hospital and medical expenses:	
Outpatient	7,851,317
Dual option product – risk adjustment	1,011,935
Net reinsurance recoveries	<u>(158,400)</u>
<b>Total Hospital and Medical Expenses</b>	<b>\$53,844,560</b>
Claims adjustment expenses	1,583,000
General administrative expenses	<u>8,675,029</u>
<b>Total Underwriting Deductions</b>	<b><u>\$64,102,589</u></b>
Net underwriting gain (loss)	1,185,328
Net investment gains (losses)	<u>170,282</u>
Net income (loss) before federal income taxes	1,355,610
Federal income taxes incurred	<u>30,868</u>
<b>Net income (loss)</b>	<b><u>\$1,324,742</u></b>



**Capital and Surplus Account**

Capital and surplus, December 31, 2003	\$2,633,649
Net income (loss)	1,324,742
Net unrealized capital gains (losses)	5,126
Change in net deferred tax asset	(506,008)
Change in nonadmitted assets	<u>646,890</u>
<b>Net change in capital and surplus for the year</b>	<b><u>\$1,470,750</u></b>
<b>Capital and Surplus, December 31, 2004</b>	<b><u>\$4,104,399</u></b>

**NOTES TO THE FINANCIAL STATEMENTS**

None.

**EXAMINATION CHANGES**

None.

**GENERAL COMMENTS AND/OR RECOMMENDATIONS****Intercompany Transactions (page 13)**

The CHP Call Center is providing various services to Heartland Regional Medical Center and related clinics without the benefit of a written agreement. The Company is directed to obtain a written agreement for the provision of the Call Center services. The agreement should clearly indicate the types of services to be provided, how charges are to be determined and manner of payment. The agreement should then be filed with the MDI for approval as required by RSMo Section 382.195 (Transactions Within a Holding Company System).

**Administrative Service Organization Fees (page 14)**

Fees received from the Administration Agreement with Heartland were reported under aggregate write-ins for other health care related revenues on the Statement of Revenue and Expenses. Per SSAP No. 47, Paragraph 5, all income and expenses related to claims, losses, premiums and other amounts received or paid on behalf of self-insured plans are to be excluded from the administrator's statement of operations. The administration fees should have been reported on line 19 (Reimbursements by uninsured accident and health plans) of Part 3 of the Underwriting and Investment Exhibit as an offset to expenses. The Company should ensure that the administration fees are properly reported on future Annual and Quarterly Statement filings.

The Administration Agreement does not address how rebates received on pharmacy claims paid on behalf of the Heartland Employee Benefit Plan should be handled. Currently, these rebates are retained by CHP. The Company should amend the Administration Agreement to clarify the handling of pharmacy rebates.

**Participating Hospital Amendments (page 15)**

The July 1, 2004 Amendment and a change to the discount rate made per a memorandum effective July 1, 2003, to the Participating Hospital Agreement with Heartland were not filed for prior approval with the MDI as required by Section 382.195 RSMo. The Company is directed to file the July 1, 2004 Amendment with the MDI and ensure amendments to intercompany agreements are properly filed in the future.

**Fidelity Bond (page 17)**

The crime coverage for Heartland and its subsidiaries on a consolidated basis does not meet the amount suggested in guidelines promulgated by the NAIC. The Company

should ensure that if the crime coverage continues to be purchased on a consolidated basis, the amount is increased to meet the suggested NAIC amounts, or the Company should obtain crime coverage sufficient to meet the NAIC guidelines as a separate entity.

**Provider Contracts (page 21)**

PharmaCare Management Services, Inc. is not licensed as a Third Party Administrator (TPA) with the Missouri Department of Insurance as required within the provisions of Section 376.1092 RSMo. The Company is directed to cause PharmaCare to comply with all the applicable Missouri laws in this regard. CHP is further directed to comply with Section 376.1084 RSMo regarding semi-annual reviews of TPAs.

The Company's contract with PharmaCare requires PharmaCare to also perform utilization reviews. However, PharmaCare is not registered as a Utilization Review Agent (URA) with the Missouri Department of Insurance (MDI) and is not covered by the exemptions listed in Section 374.500(6) RSMo, (Definitions). The Company is directed to cause PharmaCare to obtain a URA license in Missouri in order to perform its obligations under the contract.

**Custodial Agreement (page 25)**

The Company's custodial agreements with US Bank and with Commerce Bank did not contain all of the safeguard provisions specified in Part 1, Section IV of the NAIC Financial Condition Examiners Handbook. The Company should amend or restate the custodial agreement so that it contains all of the NAIC specified safeguard provisions. Until such time the agreement is brought into compliance with NAIC guidelines, it should be disclosed in General Interrogatory 23.02 of the Annual Statement for custodial agreements that do not comply with NAIC guidelines.

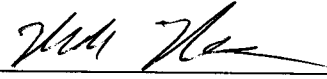
# ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Community Health Plan during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Barbara Bartlett, AFE, and Andy Balas, CFE, examiners for the Missouri Department of Insurance, participated in this examination. Karen Elsom, FSA, MAAA of the actuarial firm of Lewis and Ellis, Inc. performed an actuarial analysis as part of this examination.

# VERIFICATION


State of Missouri )  
 )  
 County of )

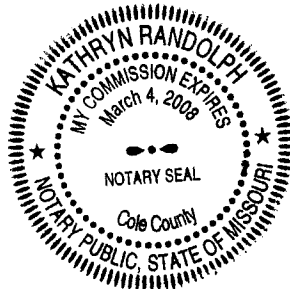
I, Mark Nance, CPA, CFE, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of the Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

  
 Mark Nance, CPA, CFE  
 Examiner-In-Charge  
 Missouri Department of Insurance

Sworn to and subscribed before me this 10<sup>th</sup> day of August, 2005.

My commission expires: \_\_\_\_\_

  
 Kathryn Randolph  
 Notary Public



# SUPERVISION


The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.



Frederick G. Heese, CFE, CPA  
Audit Manager  
Missouri Department of Insurance

Sworn to and subscribed before me this 10<sup>th</sup> day of August, 2005.

My commission expires: 03-17-2008

  
Notary Public

BEVERLY M. WEBB  
Notary Public - Notary Seal  
STATE OF MISSOURI  
Clay County  
My Commission Expires March 17, 2008



*Simply, the right choice.*  
COMMUNITY HEALTH PLAN

September 1, 2005

RECEIVED

SEP 06 2005

DIVISION  
FINANCIAL REGULATION

Mr. Kirk Schmidt, CFE, CPA  
Chief Financial Examiner  
Missouri Department of Insurance  
Harry S. Truman State Office Building, Room 530  
301 West High Street  
Jefferson City, MO 65101

Re: Examination Report of Community Health Plan for the period ending 12/31/2004.

Dear Mr. Schmidt:

Please receive this letter as our response to the examiner's findings in the above referenced report. Note that the comments are repeated (paraphrased) and the Community Health Plan (CHP) responses are in bold letters.

1. Intercompany Transactions. The CHP Call Center is providing various services to Heartland Regional Medical Center and related clinics without the benefit of a written agreement.

**CHP has drawn up an intercompany contract for the provision of Call Center services and submitted it to the Department under separate cover for review and approval.**

2. Administrative Service Organization Fees. Fees from the Administrative Agreement with Heartland were reported under aggregate write-ins for other health care related revenues... The Company should ensure that the fees are properly reported.

**CHP will report administrative service fees on Line 19 (reimbursements by uninsured accident and health plans) of Part 3 as an offset to expenses on future Annual and Quarterly Statement filings.**

3. Fidelity Bond. The crime coverage for Heartland and its subsidiaries on a consolidated basis does not meet the amount suggested in guidelines promulgated by the NAIC.

**The Company and Heartland will review the Fidelity Bond coverage for adequacy prior to the 2006 renewal.**

4. Participating Hospital Amendments. The July 1, 2004 Amendment and change to the discount rate to the agreement with Heartland was not filed for prior approval. The Company is directed to file the July 1, 2004 amendment and ensure amendments to intercompany agreements are properly filed in the future.

**CHP has filed the 2004 Amendment under separate cover. The Company will endeavor to ensure all amendments to intercompany agreements are timely filed in the future.**

5. Provider Contracts. Pharmacare Management Services, Inc. is not a licensed Third Party Administrator with the Missouri department of Insurance. Pharmacare is not registered as a Utilization Review Agent with the Missouri Department of Insurance. The Company is directed to cause Pharmacare to comply with Missouri law.

**CHP has been in contact with Pharmacare regarding licensing as a Missouri Third Party Administrator and registering as a Missouri Utilization Review Agent. Pharmacare has assured CHP that the applications have been made.**

6. Custodial Agreement. The Company's Custodial agreements with US Bank and Commerce Bank do not contain all of the safeguard provisions specified in Part 1, Section IV of the NAIC Financial Condition Examiners Handbook.

**CHP has contacted the custodial banks and requested an amendment to bring the agreements into compliance with NAIC guidelines.**

Community Health Plan requests the above responses be included in the final report as part of the public documents.

Sincerely,



Stan Vaughan  
Finance Director

CC: Lowell C. Kruse, President and CEO  
Linda S. Bahrke, Plan Administrator  
Mike Cundiff, Compliance Coordinator  
Dennis Carter, Finance Manager